



MICHAEL J. MURPHY
State Treasurer

Spring 2004

The LOCAL View

Local Option Capital Asset Lending

LOCAL Advisory Group: We couldn't do it without you

by **Michael J. Murphy**
Washington State Treasurer

This spring, we're welcoming new members and reappointing others to the LOCAL Advisory Group, which gives me occasion to talk about what groups like this mean to the Office of the State Treasurer – and how much we appreciate the service of their members.

The 13-member LOCAL Advisory Group was formed in April 1998, with 11 members appointed by associations and two members appointed by the State Treasurer. Our members serve three-year terms.

We also have an advisory group for our Local Government Investment Pool. In recent years, we got enormous help from local advisers when we established the School Bond Guarantee Program and the Statewide Custody Program.

The LOCAL Program, as the name implies, is specifically for the local governments of our state. Who better to advise us than local government finance professionals?

The people on our LOCAL advisory board know first-hand the challenges of purchasing for local governments. They know how to be innovative when resources are scarce.

They also know that LOCAL is part of the answer for cost-effective government in these precarious times. We trust our advisers to tell us loud and clear when LOCAL isn't meeting

the needs of local government. We also know that if LOCAL is working for them, they're helping to get the word out.

I've never been shy about saying local governments are our closest business partners and our most important customers – for LOCAL and for all our programs at the Office of the State Treasurer.

For the record, the new or reappointed LOCAL Advisory Group members are:

Thad Duvall, Douglas County Auditor, reappointed by the Washington State Association of County Auditors.

Stan Finkelstein, reappointed by the Association of Washington Cities.

David Griffiths, Chelan County Treasurer, appointed by WSACT. David replaces Kent Osborne.

Fred High, executive director of finance for the Kent School District, reappointed by the Washington Association of School Business Officials.

Ilene Thomson, Yakima County Treasurer, appointed by the Washington State Association of County Treasurers (WSACT). Ilene replaces Linda Wolverton.

For the complete list of our LOCAL Advisory Group, see page 2.

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Reminder, school districts: Bus financing deadline is April 1

School districts need to act soon if they are interested in replacing their pre-1977 buses through the special financing program offered by the Office of the Superintendent of Public Instruction and LOCAL. The deadline is April 1. For more information, contact OSPI or Sue Melvin of the LOCAL Program (360-902-9022).

IRS audits require longer record retention

by **William G. Tonkin**

Foster Pepper & Shefelman, PLLC

Early this year, the Internal Revenue Service issued a series of frequently asked questions and IRS answers about record retention requirements for tax-exempt bonds, the first guidance the IRS has provided on this topic.

The full IRS release can be found at www.irs.gov/bonds.

Issuers need to have and maintain pertinent records to show compliance with tax-exempt bond rules under the Internal Revenue Code, for which the IRS has an active audit program.

The code addresses arbitrage rules, such as the requirement to pay any rebate amount that may become payable to the United States if one of the rebate exceptions is not available, and the requirement that bond-financed property not be used for private business beyond limited amounts.

What should you keep?

In general, retained records should include:

- Bond transcripts;
- Documents showing the expenditures of bond proceeds;
- Documents showing how the bond-financed property is used by the public and any private users, such as copies of management contracts with any nongovernmental persons;
- Documents showing the sources of payment or security for the bonds;
- Documents pertaining to investments made from bond proceeds, including purchases and sales of securities, actual investment income from investing bond proceeds, and arbitrage rebate calculations (or records showing application of the "small issuer" exception or one of the spending exceptions to rebate).

The IRS says all these records should be kept in a manner that ensures they will be accessible to the IRS for as long as they are material. While this is typically accomplished

by keeping hard copies, records may be kept in electronic form if certain requirements are met. One requirement says that during an audit the taxpayer must retrieve and reproduce hard copies of electronically stored books and records requested by the IRS.

How long?

The IRS says records *generally* should be retained "for as long as the bonds are outstanding, plus three years after the final redemption date of the bonds."

The IRS takes this approach because it views bond records as material while bond owners are excluding from their gross income the interest from outstanding tax-exempt bonds.

Furthermore, according to the IRS, because a *refunding bond issue* is treated as replacing the original new money bonds for certain federal tax purposes, all material records relating to *both* the original new money issue *and* the refunding issue should be maintained until three years after the final redemption of *both* issues.

This view of how long records must be kept can present significant legal and practical problems for state and local governments who also are subject to state law or recommended policies on record retention that may be inconsistent with these guidelines.

One possible solution might be for an issuer to maintain a discrete set of records for its bond issues separate from its general records. However, we understand these record retention rules will be the subject of additional discussions between the IRS and issuer groups such as the Government Finance Officers Association, and other approaches may be suggested in the future.

Nonetheless, during the course of an audit of a tax-exempt bond issue, the IRS will request material records and information to determine whether the bond transaction meets the requirements of the code.

If you, as an issuer, have not maintained appropriate records, you might have difficulty demonstrating your compliance with tax law for that transaction.

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Open
State Auditor's Office
representative

GA Energy Program teams with LOCAL to save big on energy

by **Clint Lougheed**

Department of General Administration

For more than 20 years, the Washington State Department of General Administration (GA) has been helping public clients reduce their energy costs.

GA's Energy Program provides energy conservation services to municipalities, schools and state agencies throughout the state. Its record is impressive: \$90 million in completed projects; \$7.5 million annual cost savings, and electrical savings of 125 million kWh, which is enough power to serve more than 7,000 Northwest homes. In addition, GA's clients have benefited from more than \$16 million in direct grants.

Using the State Treasurer's LOCAL Program for project financing, GA has teamed up with energy service companies (ESCOs) to dramatically improve building efficiency. State of the art lighting systems, building energy-management controls, and high-efficiency HVAC systems are just a few of the improvements typically identified during a building energy audit. Improved indoor air quality is an added benefit on many projects.

Buildings aren't the only candidates for energy efficiency: Swimming pools, water treatment facilities, fish hatcheries and other energy-using systems also offer the potential for substantial energy savings.

GA has developed an innovative process for helping its clients save energy. *Energy performance contracting*, or simply performance contracting (PC), is a low-risk, streamlined (ESCOs are pre-qualified for the owner to select from) process for building

owners to identify, finance and install conservation projects. Through performance contracting, the owner needs no capital dollars, receives project cost and savings guarantees from the ESCO, and pays for all the efficiency improvements using the savings on utility bills.

LOCAL funding is typically for 10 years. Projects are always "cash neutral," meaning there is no increase in operating expenses and the owner simply uses the dollars normally sent to the local electric utility and applies them to the project loan.

One of the most attractive benefits of performance contracting is there is absolutely no

LOCAL has financed 24 energy leases totaling \$10,470,944 through GA's Energy Program.

cost to the owner if the audit fails to identify cost-effective projects. Technical assistance from GA's team of talented energy engineers is also free if the owner isn't 100 percent satisfied with the project.

For more information about GA's Energy Program, including performance contracting, building commissioning and green design, visit GA's web site at www.ga.wa.gov/energy or contact Karen Purtee at (360) 902-7194 or kpurtee@ga.wa.gov.

Clint Lougheed manages General Administration's Energy Program. The program provides energy efficiency, building commissioning and green design services to public clients throughout the state.

Quick fact

In 2003, LOCAL helped 28 local governments finance 43 equipment and real estate projects for a total of \$11.9 million.

Come see us

LOCAL representatives will staff booths at these upcoming conferences:

Washington Association of School Business Officials
May 5-7
Spokane

Association of Washington Cities
June 15-18
Ocean Shores

W. Richland taps LOCAL for new city building



"This is the third time our city has used the LOCAL program to finance a capital project," says Howard Roberts, finance director for the city of West Richland, of this new office building. "Each time, the cost of funds and other borrowing terms made the program the best fit for our city. That, plus LOCAL's knowledgeable staff, makes LOCAL a prime contender to finance our next project."

Annual LOCAL financing schedules

Real estate

Cutoff	Funding date	First payment due
Jan. 1	Mid-March	June 1 (year of issue)
April 1	Mid-June	Dec. 1 (year of issue)
July 1	Mid-September	Dec. 1 (year of issue)
Oct. 1	Mid-December	June 1 (following year)

Equipment

Cutoff	Funding date	First payment due
Feb. 1	Mid-March	June 1 (year of issue)
May 1	Mid-June	Dec. 1 (year of issue)
Aug. 1	Mid-September	Dec. 1 (year of issue)
Nov. 1	Mid-December	June 1 (following year)

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